

D.T.E. 03-72

Petition of Fitchburg Gas and Electric Light Company for approval to issue \$10,000,000 in long-term debt, pursuant to G.L. c. 164, § 14, an exemption from the requirements of G.L. c. 164, § 15, as well as the authority to receive a capital contribution of \$6,000,000 from Unitil Corporation.

APPEARANCES:

Meabh Purcell, Esq.
LeBoeuf, Lamb, Greene & MacRae, L.L.P.
260 Franklin Street, 23rd Floor
Boston, MA 02110

FOR: FITCHBURG GAS AND ELECTRIC LIGHT
COMPANY
Petitioner

Thomas F. Reilly, Attorney General
By: Wilner Borgella, Jr.
Assistant Attorney General
Utilities Division
200 Portland Street, 4th Floor
Boston, MA 02114
Intervenor

I. INTRODUCTION

On July 31, 2003, Fitchburg Gas and Electric Light Company (“Company” or “Fitchburg”) petitioned the Department of Telecommunications and Energy (“Department”), pursuant to G.L. c. 164, § 14, for approval to issue and sell long-term debt securities in the principal amount of up to \$10,000,000, with a maturity of not more than 30 years from the date of issuance and bearing interest at a fixed annual rate not to exceed eight percent (Exh. FGE-3, at 2).¹ Additionally, Fitchburg requested Department approval to receive a capital contribution from its parent corporation, Unitil Corporation (“Unitil”), in the aggregate amount of up to \$6,000,000 (id.). As part of its petition, the Company requests an exemption from the competitive bidding and advertising requirements of G.L. c. 164, § 15. The Department docketed the filing as D.T.E. 03-72.

On September 8, 2003, the Office of the Attorney General (“Attorney General”) filed a notice of intervention. Pursuant to notice duly issued, the Department conducted a public hearing at the Department’s offices on September 11, 2003. The Department held an evidentiary hearing immediately following the public hearing. In support of its petition, the Company offered the testimony of Mark Collin, senior vice-president, chief financial officer, and treasurer of Unitil; and the treasurer of Fitchburg. The evidentiary record consists of seven exhibits.

¹ In supplemental testimony filed on August 28, 2003, Fitchburg provided the specific terms of the promissory notes as a principal amount of \$10,000,000, at par, with a maturity of not more than 22 years and an interest rate of 6.79 percent (Exhs. DTE-2; FGE-1, at 3; FGE-2, at 2, sch. I).

II. DESCRIPTION OF THE PROPOSED FINANCING

A. Issuance of Long-Term Debt

The Company proposes to issue and sell unsecured long-term promissory notes in a principal amount of \$10,000,000, at par, with a maturity of not more than 22 years (Exhs. FGE-1, at 3; FGE-2, at 2, sch. I). The notes feature (1) an interest rate of 6.79 percent, payable semiannually, (2) annual sinking fund payments of \$2,000,000 beginning on the 18th anniversary of the date of issue, and (3) two optional additional sinking fund payments of \$2,000,000 beginning on the 18th anniversary of the date of issuance, allowing the Company to further reduce the life of the issue (Exhs. DTE-2; FGE-2, at 3; Tr. at 8, 11-12, 44-45). The proposed debt will be placed privately with Pacific Life Insurance Company under the auspices of the Company's investment banker, Merrill Lynch (Exh. FGE-1, at 5; Tr. at 9-10). The Company states that the proceeds from the proposed issuance of the long-term debt will be used to retire short-term debt incurred for capital expenditures (Exh. FGE-1, at 4; Tr. at 13).²

B. Exemption from G.L. c. 164, § 15

The Company contends that it would be in the public interest for the Department to grant an exemption from the competitive bidding and advertising requirements of G.L. c. 164, § 15 because there is already a measure of competition in its private placement process (Exhs. DTE-1; DTE-4; FGE-1, at 8-9; FGE-2 at 4; Tr. at 20). In addition, the

² The Company states that the short-term debt was used to provide interim financing for Fitchburg's capital construction program (Exh. FGE-1, at 3-4; Tr. at 13-14).

Company claims that its investment banker targets institutional investors who balance their portfolios with debt issuances similar in size and liquidity to the one proposed by the Company (Exh. FGE-1, at 9). Therefore, the Company argues that benefits normally inherent in advertising and competitive bidding would not be achieved in this case. Instead, the Company argues that such a process is likely to be more expensive (Exhs. FGE-1, at 9; DTE-1).

C. Capital Contribution from Unitil

In addition to the \$10,000,000 in debt sought, Fitchburg has requested authority to receive a capital contribution of \$6,000,000 from Unitil (Exh. FGE-3, at 3).³ According to the Company, the capital contribution is necessary in order for Fitchburg to maintain a balanced capital structure (Exh. FGE-2, at 5; Tr. at 14-15).

III. CAPITAL STRUCTURE OF THE COMPANY

As of May 31, 2003, the Company's total capitalization was \$86,765,976 (Exh. FGE-1, sch. C). This included \$48,000,000 in long-term debt, \$12,444,400 in common stock, \$10,182,857 in premiums paid on common stock, and \$2,163,900 in preferred stock, with the remaining balance represented by retained earnings and capital stock expense (Exh. FGE-1, schs. B, C). The corresponding capital structure ratios are 42.2 percent common equity, 2.5 percent preferred stock, and 55.3 percent total debt (Exh. FGE-1, sch. C). With the inclusion of \$27,216,569 in short-term debt, the Company's capital structure as of

³ Fitchburg explains that, because the Company was uncertain whether Department approval of the capital contribution was required, it elected to seek approval rather than run the risk of inadvertently violating Massachusetts law (Tr. at 40-42).

May 31, 2003, consisted of 66.0 percent debt, 1.9 percent preferred stock, and 32.1 percent common equity (Exh. FGE-1, at 7, sch. E)

As of May 31, 2003, the Company's utility plant in service was \$123,765,448, with accumulated depreciation of \$34,168,937, resulting in net utility plant of \$89,596,511 (Exh. FGE-1, sch. F). After the proposed issuance, the Company's total common stock, premiums, preferred stock, and long-term debt would be \$88,767,057 (id.). Therefore, the excess of utility plant over securities after the proposed issuance would be \$829,454 (\$89,596,511 minus \$88,767,057) (id.).

IV. STANDARD OF REVIEW

In order for the Department to approve the issuance of stocks, bonds, coupon notes or other types of long-term indebtedness⁴ by an electric or gas company, the Department must determine that the proposed issuance meets two tests. First, the Department must assess that the proposed issuance is reasonably necessary to accomplish some legitimate purpose in meeting a company's service obligations, pursuant to G.L. c. 164, § 14. Fitchburg Gas & Elec. Light Co. v. Department of Public Utilities, 395 Mass. 836, 842 (1985) ("Fitchburg II"), citing Fitchburg Gas & Elec. Light Co. v. Department of Public Utilities, 394 Mass. 671, 678 (1985) ("Fitchburg I"). Second, the Department must determine whether the Company has met the net plant test.⁵ Colonial Gas Company, D.P.U. 84-96 (1984).

⁴ Long-term refers to periods of more than one year after the date of issuance. G.L. c. 164, § 14.

⁵ The net plant test is derived from G.L. c. 164, § 16.

The Supreme Judicial Court has found that, for the purposes of G.L. c. 164, § 14, “reasonably necessary” means “reasonably necessary for the accomplishment of some purpose having to do with the obligations of the company to the public and its ability to carry out those obligations with the greatest possible efficiency.” Fitchburg II at 836, citing Lowell Gas Light Co. v. Department of Public Utilities, 319 Mass. 46, 52 (1946). In cases where no issue exists about the reasonableness of management decisions regarding the requested financing, the Department limits its Section 14 review to the facial reasonableness of the purpose to which the proceeds of the proposed issuance will be put. Canal Electric Company et al., D.P.U. 84-152, at 20 (1984); see e.g., Colonial Gas Company, D.P.U. 90-50, at 6 (1990).

The Fitchburg I and II and Lowell Gas cases also established that the burden of proving that an issuance is reasonably necessary rests with the company proposing the issuance, and that the Department’s authority to review a proposed issuance, “is not limited to ‘perfunctory review.’” Fitchburg I at 678; Fitchburg II at 841, citing Lowell Gas at 52. Regarding the net plant test, a company is required to present evidence that its net utility plant (original cost of capitalizable plant, less accumulated depreciation) equals or exceeds its total capitalization (the sum of its long-term debt and its preferred and common stock outstanding) and will continue to do so following the proposed issuance. Colonial Gas Company, D.P.U. 84-96, at 5 (1984).

Where issues concerning the prudence of the company’s capital financing have not been raised or adjudicated in a proceeding, the Department’s decision in such a case does not represent a determination that any specific project is economically beneficial to a company or to its customers. In such circumstances, the Department’s determination in its Order may not

in any way be construed as ruling on the appropriate ratemaking treatment to be accorded any costs associated with the proposed financing. See e.g., Boston Gas Company, D.P.U. 95-66, at 7 (1995).

Pursuant to G.L. c. 164, § 15, an electric or gas company offering long-term bonds or notes in excess of \$1,000,000 in face amount payable at periods of more than five years after the date thereof must invite purchase proposals through newspaper advertisements. The Department may grant an exemption from this advertising requirement if the Department finds that an exemption is in the public interest. G.L. c. 164, § 15. The Department has found it in the public interest to grant an exemption from the advertising requirement where there has been a measure of competition in private placement. See e.g., Berkshire Gas Company, D.P.U. 89-12, at 11 (1989); Eastern Edison Company, D.P.U. 88-127, at 11-12 (1988); Western Massachusetts Electric Company, D.P.U. 88-32, at 5 (1988). The Department also has found that it is in the public interest to grant a company an exemption from the advertising requirement when a measure of flexibility is necessary in order for a company to enter the bond market in a timely manner. See e.g., Western Massachusetts Electric Company, D.P.U. 88-32, at 5 (1988). However, G.L. c. 164, § 15 requires advertising as the general rule, and waiver cannot be automatic, but must be justified whenever requested.

V. ANALYSIS AND FINDINGS

A. Long-Term Debt

The Company proposes to issue and sell unsecured long-term promissory notes in a principal amount of \$10,000,000, at par, with a maturity of not more than 22 years

(Exhs. FGE-1, at 3; FGE-2, at 2, sch. I). The proceeds of the sale will be applied to the retirement of short-term debt incurred by the Company to finance the expansion or replacement of investments in its utility operations, which is a legitimate purpose in meeting the Company's utility service obligations. Fitchburg Gas and Electric Light Company, D.T.E. 01-43, at 6 (2001); Southern Union Company, D.T.E. 01-32 (2001), at 10; Berkshire Gas Company, D.P.U. 98-129, at 8 (1999). Accordingly, the Department finds that the proposed issuance is reasonably necessary to accomplish a legitimate purpose in meeting the Company's service obligations in accordance with G.L. c. 164, § 14.

In regard to the net plant test, the Department requires companies to demonstrate that their net utility plant equals or exceeds their total capitalization. Colonial Gas Company, D.P.U. 84-96, at 5 (1984). If a company's financing proposal fails to meet this requirement, G.L. c. 164, § 16 authorizes the Department to prescribe such conditions and requirements as it deems best adapted to make good within a reasonable time period the capital stock impairment. The record demonstrates that the Company's total capital stock and long-term debt will not exceed the Company's net utility plant following the issuance and sale of the long-term debt securities (Exh. FGE-1, sch. F). Accordingly, the Department finds that the Company's issuance of up to \$10,000,000 in long-term securities meets the net plant test as provided in G.L. c. 164, § 16.

Issues concerning the prudence of the Company's capital financing have not been raised in this proceeding and the Department's decision in this case does not represent a determination that any project is economically beneficial to the Company or its customers.

The Department's determination in this Order is not in any way to be construed as a ruling relative to the appropriate ratemaking treatment to be accorded any costs associated with the proposed financing.

B. Exemption from G.L. c. 164, § 15

The Company has demonstrated that it selected an investment banker with broad experience in the bond market, access to potential institutional investors, and significant knowledge about the Company's financial needs (Exh. FGE-1, at 9; Tr. at 20-21).

The Company's investment banker solicited institutional investors for private placement of the issue through a competitive process (Exhs. DTE-4; FGE-1, at 9-10). Based on the nature of the issuance sought, a public placement of the proposed issuance would be considerably more expensive, primarily due to the relatively small size of the issuance and the higher fixed cost of a public offering (Exhs. DTE-1; FGE-1, at 9; FGE-2, sch. H at 1-2).⁶ In light of the foregoing considerations, the Department finds that a competitive bidding process would not provide any advantages for ratepayers over those offered by the Company's private placement process, and that a competitive bidding process could result in higher interest rates.

Therefore, the Department finds that it is in the public interest to exempt the Company from the competitive bidding and advertising requirements in G.L. c. 164, § 15.

⁶ According to Fitchburg's investment banker, a public offer would need to have a face value of at least \$200,000,000 in order to provide sufficient liquidity for investors (Exh. FGE-2, sch. H at 1). Moreover, even if a public placement was possible, the Company's investment banker estimates that the required coupon rate would be approximately 8.34 percent, versus the 6.79 percent achieved through private placement (*id.*).

C. Capital Contribution

The Department has previously noted that the financing statutes contained in G.L. c. 164 were designed to protect both ratepayers and the investing public from the effects of fraudulent stock or bond transactions. Massachusetts-American Water Company, D.P.U. 95-41, at 9 (1995).⁷ The knowing and voluntary act of a sole shareholder, such as Unitil, which itself is not a regulated gas, electric or water company, to infuse equity capital into its wholly-owned subsidiary does not offend the protective purpose of these statutes. Id. Therefore, the arrangement for infusion of capital by Unitil to Fitchburg, which capital contribution will not involve the sale or issuance by the Company, does not constitute a financial proceeding requiring further approval by the Department under G.L. c. 164, §§ 10, 14, and 17A. In reaching this conclusion, the Department makes no findings relative to the propriety of the resulting common equity structure of Fitchburg, or its effect on the Company's weighted cost of capital.

⁷ With regard to capital contributions, G.L. c. 164, § 10, states in pertinent part that “[a] corporation subject to this chapter shall, upon an issue of capital stock . . . notify the [D]epartment of such issue.” General Laws c. 164, § 14, states in pertinent part that “companies shall issue only such amounts of stock and bonds, and of coupon notes and other evidences of indebtedness . . . as the [D]epartment may . . . vote is reasonably necessary for the purpose for which such issue of stock and bonds, and of coupon notes and other evidences of indebtedness has been authorized.” Finally, G.L. c. 164, § 17A states in pertinent part that:

No . . . company shall, except in accordance with such . . . regulations as the [D]epartment shall . . . prescribe, loan its funds to, guarantee or endorse the indebtedness of, or invest its funds in the stocks, bond, certificates of participation or other securities of, any corporation, association or trust unless the said loan, guarantee or endorsement, or investment is approved . . . by the [D]epartment.

VI. ORDER

Accordingly, after due notice, hearing and consideration, the Department:

VOTES: That the issuance and sale by Fitchburg Gas and Electric Light Company of up to \$10,000,000 aggregate principal amount of long-term notes at par, by private sale for cash to an institutional investor or investors, is reasonably necessary for the purposes for which such issuance and sale has been authorized, pursuant to G.L. c. 164, § 14; and

VOTES: That the issuance of the long-term debt is in accordance with G.L. c. 164, § 16 in that the fair structural value of the Company's property, plant, and equipment held by the Company, will exceed its outstanding stock and long-term debt; and

VOTES: That it is in the public interest that the issuance and sale of said long-term debt be exempt from the requirements of G.L. c. 164, § 15; and it is

ORDERED: That the Department approves and authorizes the issuance and sale by Fitchburg Gas and Electric Light Company, in conformity with all the provisions of law relating thereto, of up to \$10 million principal amount of long-term debt securities with a maturity no later than 22 years from issuance, which debt securities carry an interest rate of 6.79 percent; and it is

FURTHER ORDERED: That the Fitchburg Gas and Electric Light Company be exempt from all of the requirements of G.L. c. 164, § 15, as amended, with respect to the issuance and sale of said long-term debt securities; and it is

FURTHER ORDERED: That the net proceeds from such sale of said long-term debt securities shall be used to retire Fitchburg Gas and Electric Company's existing short-term debt, and it is

FURTHER ORDERED: That the Secretary of the Department will within three days of the issuance of this Order cause a certified copy of it to be filed with the Secretary of the Commonwealth.

By Order of the Department

/S/_____
Paul G. Afonso, Chairman

/S/_____
James Connelly, Commissioner

/S/_____
W. Robert Keating, Commissioner

/S/_____
Eugene J. Sullivan, Jr., Commissioner

/S/_____
Deirdre K. Manning, Commissioner

Appeal as to matters of law from any final decision, order or ruling of the Commission may be taken to the Supreme Judicial Court by an aggrieved party in interest by the filing of a written petition praying that the Order of the Commission be modified or set aside in whole or in part.

Such petition for appeal shall be filed with the Secretary of the Commission within twenty days after the date of service of the decision, order or ruling of the Commission, or within such further time as the Commission may allow upon request filed prior to the expiration of twenty days after the date of service of said decision, order or ruling. Within ten days after such petition has been filed, the appealing party shall enter the appeal in the Supreme Judicial Court sitting in Suffolk County by filing a copy thereof with the Clerk of said Court. (Sec. 5, Chapter 25, G.L. Ter. Ed., as most recently amended by Chapter 485 of the Acts of 1971).